



National Energy
Board

Office national
de l'énergie

Reasons for Decision

Land Matters Consultation Initiative Stream 3

RH-2-2008

May 2009

**Pipeline Abandonment - Financial
Issues**

Canada



National Energy Board

Reasons for Decision

In the Matter of

**Land Matters Consultation
Initiative Stream 3**

Financial Issues related to Pipeline
Abandonment

RH-2-2008

May 2009

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Chapter 1

Disposition by the National Energy Board

File ADV-PE-LandMC 02
26 May 2009

To: All Parties to RH-2-2008 and All Pipeline Companies

**Hearing Order RH-2-2008 - Land Matters Consultation Initiative Stream 3
Pipeline Abandonment – Financial Issues
Board Decision**

Background

In January 2008, the National Energy Board (Board) identified a proposed approach for the Land Matters Consultative Initiative (LMCI), consisting of four distinct topic streams. One of the four topic streams, Stream 3, is “Pipeline Abandonment – Financial Issues”. The Board indicated that the key issue to be considered in respect of that topic stream is the following:

What is the optimal way to ensure that funds are available when abandonment costs are incurred?

For LMCI Stream 3, the Board decided to convene a public hearing to consider the financial issues related to pipeline abandonment. Pursuant to subsection 15(1) of the *National Energy Board Act* (NEB Act), the Board authorized three members to conduct the hearing and to report and make recommendations to the Board in respect of the decision of the Board to be made on the issues in the hearing (the Panel).

The Panel conducted a public hearing, the oral portion of which was heard in January 2009. The Panel’s Report and Recommendations were presented to the Board in April 2009, and are attached as Appendix I to this Decision.

Board Decision

The Board, having received and considered the Report and Recommendations, has adopted the Panel’s Report and Recommendations, including the Framework and Action Plan set out in the Report, as the decision of the Board in LMCI Stream 3. As a result, all pipeline companies regulated under the NEB Act are directed to comply with the steps set out in the Framework and Action Plan.

The Board will be assessing each filing made by regulated companies, including Group 2 companies, in light of the principles and considerations set out in the Report, as well as the

requirements of the NEB Act. If required, additional information may be sought to aid the Board in its assessment of the filing and further direction may be issued to a regulated company.

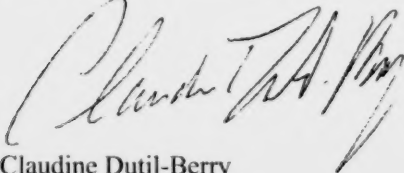
The Board has assigned dates to the deadlines set out in the Action Plan, Table 4-1 of the Panel's Report. Accordingly, the Board has attached a revised Action Plan, Table 4-1, as Appendix A.

Next Steps

Regulated companies are directed to serve a notice of this decision and information as to the location of this decision on the Board's Internet Site [www.neb-one.gc.ca, click on the Land Matters Consultation Initiative icon on the right-hand side of the page, scroll down and select Stream 3, and then click on the News Release and Decision dated 26 May 2009] on their shippers and interested parties, including parties to their latest toll decision or settlement.

Regulated companies and Parties to the RH-2-2008 proceeding will be advised by letter of the date of the Technical Conference regarding the Base Case Assumptions. Any other interested persons who wish to be advised of the upcoming Technical Conference are invited to contact Erin Dutcher, Regulatory Officer, at 403-299-2782 or toll-free at 1-800-899-1265 to indicate their interest and provide their contact information.

Yours truly,

A handwritten signature in dark ink, appearing to read "Claudine Dutil-Berry". The signature is fluid and cursive, with the first name being more prominent.

Claudine Dutil-Berry
Secretary of the Board

Attachments

**Table 4-1
Action Plan**

Action	Objective	Participants	Timing
1. RH-2-2008 Decision released	Discussion of principles, high level Framework, Action Plan, Preliminary Base Case	NEB	May 2009
2. Board Technical Conference on Preliminary Base Case	Potential refinements to Preliminary Base Case	Group 1 and Group 2 companies that wish to attend, and any other interested person	November 2009
3. Release of Refined Base Case	Base Case issued for company use	NEB	February 2010
4. (a) Group 1 companies each prepare and file an estimate of abandonment costs and the amount required to be set aside using the Base Case assumptions OR (b) Group 1 companies each prepare and file, for approval , an estimate of abandonment costs and the amount required to be set aside using pipeline-specific assumptions or a combination of pipeline-specific and Base Case assumptions	Filing of preliminary estimates using Base Case or pipeline-specific assumptions	Group 1 companies	No later than 31 May 2011
5. NEB consideration of Group 1 companies' preliminary estimates that use pipeline-specific assumptions or a combination of pipeline-specific and Base Case assumptions	NEB decisions on Group 1 companies' preliminary estimates	NEB	By 31 May 2012

6. Group 1 companies each develop and file, for approval , a proposal for collection of funds and a proposed process and mechanism to set aside the funds [can be combined with step 4 and filed by 31 May 2011]	Filing of proposed collection mechanisms and proposed set aside mechanisms	Group 1 companies	No later than 30 November 2012
7. Group 2 companies each prepare and file an estimate of abandonment costs and the amount required to be set aside using either the Base Case or pipeline-specific assumptions	Filing of preliminary estimates using Base Case or pipeline-specific assumptions	Group 2 companies	No later than 30 November 2011
8. Group 2 companies that charge tolls each develop and file a proposal for collection of funds [can be combined with step 7 and filed by 30 November 2011]	Filing of proposed collection mechanisms	Group 2 companies that charge tolls	No later than 30 November 2012
9. Group 2 companies each file with the Board a proposed process and mechanism to set aside funds [can be combined with steps 7 or 8, and filed at the earliest applicable date]	Filing of proposed set aside mechanisms	Group 2 companies	No later than 31 May 2013
10. NEB consideration of Group 1 companies' proposals for collection and set aside mechanisms	NEB decisions on Group 1 companies' mechanisms for collection and set aside of funds	NEB	By 31 May 2014

Appendix I

NEB Section 15 Report

National Energy Board

**Report and
Recommendations
Pursuant to Section 15
of the *National Energy
Board Act***

In the Matter of

**Land Matters Consultation
Initiative Stream 3**

Financial Issues related to Pipeline
Abandonment

RH-2-2008

April 2009

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Abbreviations

Board or NEB	National Energy Board
CAPLA	Canadian Alliance of Pipeline Landowners' Associations
CAPP	Canadian Association of Petroleum Producers
CEPA	Canadian Energy Pipeline Association
Enbridge	Enbridge Pipelines Inc.
KMC	Kinder Morgan Canada Inc.
LMCI	Land Matters Consultation Initiative
NEB Act	<i>National Energy Board Act</i>
Panel	National Energy Board members appointed pursuant to subsection 15(1) of the <i>National Energy Board Act</i> to prepare a report and recommendations
Pouce Coupé	Pouce Coupé Pipe Line Ltd.
TransCanada	TransCanada PipeLines Limited, Nova Gas Transmission Ltd., Foothills Pipe Lines Ltd., Trans Québec & Maritimes Pipeline Inc., TransCanada Keystone Pipeline GP Ltd.
Westcoast	Westcoast Energy Inc., carrying on business as Spectra Energy Transmission

Glossary of Terms

Abandon	To permanently cease operation such that the cessation results in the discontinuance of service.
Decommission	To permanently cease operation such that the cessation does not result in the discontinuation of service, for example, when a tank is removed from operation on a pipeline and the pipeline continues to operate without the tank.
Depreciation	A non-cash expense charged against earnings to write-off the cost of an asset during its estimated useful life.
Group 1 Company	In general, Group 1 companies are those with more extensive systems and as such are subject to a greater degree of regulatory oversight on financial matters than Group 2 companies.
Group 2 Company	Group 2 companies tend to have smaller systems, with fewer shippers and are subject to a lighter degree of regulatory oversight on financial matters; generally, they are regulated on a complaints basis.
Intergenerational Equity	A broad principle that users in any period are generally required only to pay for the costs of providing them with services in that period.
MH-1-96	NEB proceeding on an application by Murphy Oil Company Ltd. on behalf of Manito Pipelines Ltd. to abandon certain facilities.
Orphan Facility	An oil or gas facility that has, or is deemed to have, no legally responsible and financially viable owner.
Paragraph 74(1)(d)	A paragraph of the NEB Act requiring leave of the Board before a company abandons the operation of its pipeline.
Perpetual Maintenance	The ongoing use of methods to maintain an abandoned pipeline to avoid collapse, subsidence, corrosion or other adverse impacts. This is sometimes referred to as continuing maintenance.
Residual Risk	The risk, remaining at the completion of the pipeline life, related to the adequacy of funding to cover the entire cost of the abandonment activities.

Retirement	An accounting term for when an asset, whether it is replaced or not, is otherwise removed from pipeline service.
Salvage	The value at removal of pipe and facilities.
Stream 4	The stream of the LMCI dealing with physical issues related to pipeline abandonment.
Terminal Negative Salvage	The costs incurred in the abandonment of pipeline facilities less any value realized from the disposition of such facilities.
Zones 1 and 2	Toll zones for Westcoast's gathering and processing facilities.
Zones 3 and 4	Toll zones for Westcoast's transmission facilities.

Recital and Appearances

IN THE MATTER OF the *National Energy Board Act* (NEB Act) and the Regulations made thereunder;

IN THE MATTER OF the Land Matters Consultation Initiative (LMCI) Stream 3, Pipeline Abandonment – Financial Issues; and

IN THE MATTER OF National Energy Board Hearing Order RH-2-2008.

HEARD in Calgary, Alberta on 20, 21, 22, 23, 26 and 28 January 2009;

BEFORE SECTION 15(1) PANEL:

S. Leggett	Presiding Member
K.M. Bateman	Member
L. Mercier	Member

Appearances

Participants

Witnesses

D. Crowther
R. Power

Alliance Pipeline Ltd.

C. Worthy

BP Canada Energy Company

D. Crowther
M. Yohemas

Enbridge Pipelines Inc.

P. Douvris
M. Hrynchyshyn
R. Mansell

L.R. Aufricht

Imperial Oil Resources

P. Forrester
M. Novak

Kinder Morgan Canada Inc.

B. McClellan
S. Stoness

P. Jeffrey
P. Khan

Pouce Coupé Pipe Line Ltd.

P. Robertson

D. Davies
R. Sirett

Spectra Energy Transmission (Westcoast)

M. Bootle
T. Curry
A. Parmar
D. Rae

D. Armstrong

Suncor Energy Marketing Inc.

S. Denstedt N. Berge M. Keen	TransCanada PipeLines Limited, NOVA Gas Transmission Ltd., Foothills Pipe Lines Ltd., TransCanada Keystone Pipeline GP Ltd., Trans Québec & Maritimes Pipeline Inc.	A. Leong J. Van der Put
P.G. Vogel J. Goudy	Canadian Alliance of Pipeline Landowners' Associations	A. Cheung D. Core K. Habermehl R. Kraayenbrink J. Ness C. Storey P. Teevens
N.J. Schultz	Canadian Association of Petroleum Producers	B. Jardine H. Johnson
C. King	Alberta Department of Energy	
J. Saunders P. Johnston	National Energy Board	

Chapter 1

Introduction

1.1 Background

In the fall of 2007, the National Energy Board (the Board or the NEB) announced that, as part of its review of key land issues, it had decided to establish the Land Matters Consultation Initiative (LMCI). The decision resulted from the Board's desire to support continual improvement related to land matters, and confirmed the Board's belief that constructively engaging interested people and organizations would be an effective approach to meet this goal. The Board issued its LMCI Approach on 25 February 2008, which identified potential outcomes that were intended to improve how land matters are appropriately and effectively included in the Board's public interest considerations. The Board also noted that the LMCI would provide a forum for all interested parties and the Board to engage in dialogue and generate options related to land matters for the Board's review.

The Board considered the LMCI topics in four streams:

- Stream 1: Company Interactions with Landowners;
- Stream 2: Improving the Accessibility of NEB Processes;
- Stream 3: Pipeline Abandonment – Financial Issues; and
- Stream 4: Pipeline Abandonment – Physical Issues.

For Stream 3, the Board noted two key principles fundamental to its future decisions with respect to the financial matters related to pipeline abandonment. They are:

1. Abandonment costs are a legitimate cost of providing service and are recoverable upon Board approval from users of the system.
2. Landowners will not be liable for costs of pipeline abandonment.

The Board stated that the key issue to be decided related to the financial aspect of abandonment is: What is the optimal way to ensure that funds are available when abandonment costs are incurred? The Board also indicated that the potential outcomes of Stream 3 are:

- *Development of a set of principles which will guide the Board in its future decisions with respect to the financial matters related to pipeline abandonment;*
- *Preliminary mechanism to begin setting aside funds for abandonment costs is identified;*
- *Identification of technical abandonment assumptions to be used to estimate abandonment costs; and*
- *An action plan is developed to move forward on remaining financial issues including issues unique to each pipeline company.*

In March 2008, the Board released a Discussion Paper for Stream 3 that summarized the past relevant documents, discussed practices in other jurisdictions, and identified the proposed financial issues that would need to be decided related to abandonment funding. One of those past documents was the 1985 NEB staff paper entitled "Background Paper on Negative Salvage Value". This paper provides useful background information in the Board's continuing examination of abandonment issues.

1.2 Hearing Process

For LMCI Stream 3, the Board decided to convene a public hearing to consider the financial issues related to pipeline abandonment. In terms of the governance for Stream 3, the Board authorized, pursuant to subsection 15(1) of the *National Energy Board Act* (NEB Act), three members (the Panel) to conduct this hearing and to report and make recommendations to the Board in respect of the decision of the Board to be made on the issues in this hearing.

On 3 March 2008, the Panel issued Hearing Order RH-2-2008 for LMCI Stream 3, setting out the procedures to be followed for a public hearing to begin on 17 June 2008. As part of those procedures, the Panel decided to convene a pre-hearing conference on 3 April 2008 to discuss with interested parties any proposed additions or changes to the List of Issues as well as a number of procedural issues.

On 26 March 2008, the Panel issued a letter to parties indicating that, having received comments on the hearing timetable from parties representing a wide range of interests, the Panel decided to postpone the commencement of the hearing to a later date. The Panel announced that the exact date for the hearing and corresponding revisions to the timetable of events would be discussed at the 3 April 2008 pre-hearing conference.

On 15 April 2008, the Panel issued its Pre-hearing Conference Report to all parties. It issued its ruling on the List of Issues and Timetable of Events on 21 April 2008. In its ruling, the Panel announced that the oral portion of the hearing would commence on 20 January 2009 at a location to be determined later. In response to suggestions by participants at the conference that one or more procedural or technical conferences may be beneficial to the hearing process, the Panel set deadlines by which parties could request additional conferences.

On 8 October 2008, the Canadian Energy Pipeline Association (CEPA), on behalf of itself and its member companies, suggested that the "Mechanics and Governance of establishing Environmental Trusts for pipeline abandonment funds" be part of the agenda for a technical conference. The Panel subsequently scheduled a conference for 30 October 2008 to deal with CEPA's suggestion plus two procedural matters; namely, the location of the hearing and the order of appearances for evidence, cross-examination and final argument. The Panel issued its Conference Report on 5 November 2008 and, on 21 November 2008, the Panel provided its ruling on the procedural issues discussed at the conference.

Five pipeline companies, Enbridge Pipelines Inc. (Enbridge), Kinder Morgan Canada Inc. (KMC), Pouce Coupé Pipe Line Ltd. (Pouce Coupé), TransCanada PipeLines Limited (TransCanada) and Westcoast Energy Inc. (Westcoast), and two associations, the Canadian Alliance of Pipeline Landowners' Associations (CAPLA) and the Canadian Association of

Petroleum Producers (CAPP), submitted evidence in this proceeding. A number of other persons either intervened but did not submit evidence, or participated by submitting a letter of comment.

The Panel heard oral evidence between 20 and 26 January 2009, and final argument on 28 January 2009, in Calgary, Alberta.

1.3 List of Issues

In its RH-2-2008 Hearing Order, as amended, the Panel identified, but did not limit itself to the following issues for discussion in the proceeding:

1. Should the Board require pipeline companies to set aside funds to cover future abandonment costs?
 - a. What are the implications on all persons impacted, including shippers, producers, regulated companies, governments, landowners and other members of the public, of requiring or of not requiring pipeline companies to set aside funds to cover future abandonment costs?
 - b. If funds are required to be set aside, what mechanisms should be considered and what are the pros and cons of each mechanism?
 - c. If funds are required to be set aside, should all pipeline companies under the Board's jurisdiction be required to set aside these funds?
2. If companies are required to set aside funds, what information and assumptions are necessary to create preliminary estimates for future abandonment costs? For example:
 - a. What technical and financial assumptions should be used to create preliminary cost estimates?
 - b. What process would be appropriate for the Board to consider preliminary estimates for individual pipelines?
 - c. What should be the process for refining the estimates over time?
3. If companies are required to set aside funds, when should the collection of funds commence?
 - a. Should all pipeline companies under the Board's jurisdiction be required to start collecting funds for abandonment at the same time, (e.g. by calendar date or year of pipeline life)?
4. If companies are required to set aside funds, how should the funds be set aside?
 - a. Should they be collected from shippers through annual payments or per unit tolls, or set aside through insurance, or should some other method be used?
 - b. If the funds are collected through the tolls of a pipeline company, should they be collected as a component of depreciation or separately?

5. If companies are required to set aside funds, how should the funds be governed? For example:
- a. Should the funds be maintained in a separate trust account, commingled with a company's general corporate revenue, maintained and administered by a third party or maintained in another manner?
 - b. Should a portion of the funds be pooled for use across industry (e.g. orphan pipeline fund)?
 - c. Should reporting requirements for the funds be established, and if so, what should they be?
 - d. Should the regulated portion of a company be insulated from the non-regulated business with respect to abandonment costs, and if so, how?
 - e. How would a company access the funds?
 - f. What would be the appropriate time to access funds (e.g. only at the end of a pipeline's life or also for interim retirements)?
 - g. Who should control access to the funds – a company, a corporate third party, a regulator?
 - h. What investment restrictions should be placed on the funds collected, if any?
 - i. What taxation issues arise from the collection of funds and how could they be addressed?
 - j. What should happen to any funds collected to abandon a pipeline regulated by the NEB which then becomes subject to provincial jurisdiction, either after abandonment or through a transfer to a provincially-regulated company?
 - k. Should there be surplus funds collected, what should be the final disposition of those funds?
6. How best should the risks and uncertainties inherent in determining future abandonment costs and revenues be managed or mitigated?
- a. Who should bear the risk/reward of trust account performance?
 - b. Who should bear the risk/reward of under/over collection of funds?
7. What is the Board's mandate under the current legislation to require the collection of abandonment costs as a component of a company's revenue requirement?

Chapter 2

Submissions of Parties

This chapter summarizes the submissions of parties and generally follows the order of the List of Issues found in section 1.3.

2.1 Should the Board require that funds be set aside for abandonment?

All of the parties that filed evidence in this proceeding agreed with the key principle in the Board's 25 February 2008 letter, which stated that landowners will not be liable for costs of pipeline abandonment. Enbridge submitted that whatever funding provision was made for abandonment costs and liabilities, it must be sufficient so that landowners and shareholders would not be left bearing any liability. All parties agreed that pipeline companies have an obligation to ensure sufficient funds will be in place to pay for all costs of abandonment.

As a result, all parties who actively participated in the LMCI hearing agreed that abandonment funds should be set aside. There were various opinions on how and when such funds should be collected and set aside.

Enbridge, KMC, Pouce Coupé and TransCanada, as well as CAPLA and CAPP, stated in their evidence that they are in favour of the collection of monies to fund abandonment costs from pipeline users, as these costs are a legitimate cost of providing service and should be recoverable from shippers.

Westcoast submitted that it should not be required to collect and set aside funds to cover future abandonment costs. Westcoast stated that, with respect to its transmission assets (Zones 3 and 4), it would make an application to the Board to collect and set aside funds after recognizing the liability according to accounting rules and standards. In addition, Westcoast made a distinction between its gathering and processing facilities (Zones 1 and 2) and its transmission facilities stating that each should be treated differently. Westcoast submitted that, for competitive reasons, the Board should not require collection for Zones 1 and 2, but rather allow Westcoast to manage its internal accounts appropriately to ensure it can fund its liabilities. While Westcoast did not think collection should be mandated for any of its facilities, it submitted collection could occur on its transmission assets at the same time collection is required on other federally regulated transmission lines. Further discussion of parties' submissions on competitive impacts of collection follows below.

KMC, Pouce Coupé, TransCanada and CAPLA favoured earlier rather than later collection, although the definition of what was meant by "earlier" and "later" varied between the parties. TransCanada proposed that during the time it takes to prepare an abandonment study, collection could begin with a nominal amount based on an agreed-to percentage of each pipeline's annual revenue requirement.

KMC and TransCanada raised concerns regarding the effect of collection on intergenerational equity. KMC stated that a common principle of rate setting is that the pipeline should collect costs such that one generation of customers does not subsidize a different generation of customers. TransCanada submitted that funds to cover abandonment costs should be collected sufficiently in advance of abandonment so as not to unfairly burden those shippers who contract for service towards the end of a pipeline's economic life.

Competitive and Other Impacts of Collection

All pipeline companies and CAPP raised concerns regarding the impacts on competitive dynamics of collection of abandonment funds from shippers. KMC, Pouce Coupé and TransCanada submitted that the framework governing the funding for abandonment should be consistently applied to minimize any economic inefficiencies or material impacts, which could cause competitive advantages or disadvantages. Enbridge stated that the abandonment surcharge alone would not determine competitive impacts. In its view, there are other, often more significant, components than tolls that impact competitiveness, such as market prices. CAPLA suggested that if collection started early enough, changes to competitive dynamics could be avoided.

Westcoast submitted that competition with provincially regulated service providers was the entire justification for its position that it should not be required to collect abandonment funds in its gathering and processing business. Westcoast stated that its gathering and processing business is unique in Canada as it is the only one federally-regulated under the Framework for Light-Handed Regulation¹. For Zones 1 and 2, the market sets the tolls, not cost-based regulation, and Westcoast negotiates tolls with shippers in a competitive market. Westcoast argued that it bears the full utilization risk associated with these facilities, and does not collect any specific costs in its Zone 1 and 2 tolls. Further, it argued that it could not increase its tolls above market value to collect an additional cost, as this would put it at a competitive disadvantage to others in the gathering and processing business. Westcoast submitted that the Board should not require collection for Zones 1 and 2, but rather allow Westcoast to manage its own accounts appropriately to ensure it can fund its liabilities.

Another concern raised by some industry parties regarding the effect of requiring collection was that collection could result in an increase in costs to shippers. This could lead to a decline in utilization, reducing the ability of the pipeline to collect adequate funds. A decline in use could lead to remaining shippers being charged more and a resulting further decline in use, until the point where the pipeline has few or no shippers to cover the higher and higher tolls required (colloquially called a "death spiral"). However, some parties, such as Enbridge, TransCanada, KMC and CAPP, recognized that this concern could be mitigated by beginning collection earlier. With earlier collection, the increase in costs to shippers could be more modest and thus may prevent a decline in utilization and reduce the risk of creating a death spiral.

¹ National Energy Board, RHW-1-98, Key Documents Related to the Board's Decision on the Framework for Light-Handed Regulation, June 1998

2.2 Preliminary Estimates

Many parties indicated that various technical and financial assumptions were required in order to prepare preliminary estimates of the funds required for abandonment. Some of the technical and financial assumptions identified by parties included:

- the physical method of abandonment;
- technology available at the time of abandonment;
- legislative requirements;
- environmental impacts and subsequent remediation requirements;
- estimated salvage value;
- administrative costs;
- cost escalation factors;
- expected investment yield on funds invested;
- timing of abandonment;
- income tax implications; and
- the effect of collection of funds on existing toll settlements.

Enbridge, Pouce Coupé, TransCanada and CAPP all submitted that the income tax treatment of funds collected from shippers and details of a trust fund mechanism with its associated investment policy should be resolved prior to beginning collection of funds. Resolution of these matters would ensure tax efficient use of funds. TransCanada stated that if revenues collected to fund abandonment costs are taxable when collected, then the amount collected has to be increased by the tax component, plus an amount resulting from expenses being non-deductible at the end of the pipeline's life (because there is no taxable income against which expenses can be deducted). TransCanada acknowledged that tax efficient collection issues must be balanced with other factors and principles.

Several parties submitted that the LMCI Stream 4 process would need to be completed before the technical assumptions necessary for cost estimation could be made. CAPLA proposed a default technical assumption of removal of all large diameter pipelines in agricultural land or perpetual maintenance until all abandoned pipelines in a corridor have been removed. CAPLA supported the default abandonment option for the same reasons identified by the NEB in its 1985 staff paper entitled "Background Paper on Negative Salvage Value"; for example, to reduce the risk of subsidence, corrosion contamination and the creation of water conduits. All other parties viewed full removal as an overly conservative assumption.

All parties who filed evidence agreed that estimates should be refined over time. While the frequency of review ranged from every ten years to annually, the most common suggestion for the reviews of estimates was every five years. TransCanada suggested that the frequency of review could be increased as the time of abandonment approaches.

2.3 Timing of Collection

The submissions of parties on the timing for collecting abandonment funds centered on four themes: commencement of collection, deferral, nominal amount and Group 1 vs. Group 2 companies.

Commencement of Collection

Enbridge stated that a number of issues would need to be resolved before any collection for abandonment should occur. These issues included:

- tax status and treatment of abandonment fund contributions and earnings;
- specifics of a trust or other such structure;
- governance and reporting;
- investment guidelines;
- access to funds;
- assumptions regarding the requirement for, and method of, facility abandonment; and
- collection monitoring and adjustment mechanisms.

Enbridge also proposed that the Board establish a methodology that incorporated flexibility for companies to apply for the deferral of collection.

KMC supported an expeditious process that would have the recovery of abandonment costs commence at the earliest opportunity, with all pipelines beginning collection within three years following the conclusion of LMCI Stream 4. In KMC's view, this would provide adequate time for companies to prepare preliminary estimates on abandonment costs and prepare the mechanisms for administering, collecting, managing and reporting on the funds. This would also allow affected regulatory authorities to establish and provide the necessary regulatory oversight associated with abandonment fund collection. KMC was of the view that even if the tax issues are not resolved, funds should be collected.

Pouce Coupé stated that the collection of funds should commence immediately for all pipeline companies, subject to the reasonable time required to conduct the requisite assessment. This assessment would include an indication of the steps that would have to be taken for abandonment, the costs of those steps and the toll surcharge required to cover the costs. According to Pouce Coupé, earlier collection would provide the company with a longer collection period and perhaps more surety that the funds required would be collected.

TransCanada suggested that collection should begin as soon as practical. TransCanada defined "as soon as practical" as the time required to put a trust mechanism in place, address tax efficiency, prepare abandonment cost estimates, and deal with issues such as existing toll settlements.

According to Westcoast, collection should not occur until the amount of costs and the time when the costs will be incurred can be reasonably determined. Westcoast stated that its NEB-regulated

gathering, processing and transmission assets have an indeterminate life and submitted, as a result, that collection should not be required by Westcoast at this time.

CAPLA stated that collection of abandonment reserves should begin immediately, so that landowners do not bear the risk of pipelines being abandoned before sufficient reserves have been established. CAPLA stated that "immediately" means, "as soon as a decision is made at this hearing".

CAPP submitted that all pipelines should be subject to the same requirements and the commencement of collection of funds should not be based on the vintage of a pipeline. In addition, the collection of funds should not begin until the Department of Finance amends the *Income Tax Act* (discussed further in Section 2.5).

Deferral

According to Enbridge, collection of abandonment funds should commence when a reasonably foreseeable date of abandonment and an estimate of costs can occur. Many pipeline assets have sufficiently long economic lives and their abandonment is not reasonably foreseeable within a timeframe that has any practical consequence. As a result, Enbridge suggested that any abandonment funding collection mechanism incorporate flexibility to accommodate differences among pipeline facilities in key parameters, such as expected economic life, and permit the Board to authorize deferral of fund collection by a pipeline.

Enbridge submitted that deferrals would not cause competitive impacts as competing pipelines would have similar supply and market demand fundamentals and would therefore be in a similar position to receive a deferral from the Board.

KMC submitted that deferred collection would be inconsistent with the regulatory principle of intergenerational equity, could cause potential competitive disadvantages between pipelines and could pose a greater risk of leaving taxpayers, landowners and government with the costs of abandonment. It disagreed with waiting until abandonment was reasonably foreseeable because there is significant risk that the pipeline life could be truncated and there would not be monies available to remove the facilities at that time. KMC cited potential changes in American or Canadian government energy policy as adding to the risk of pipeline life truncation.

KMC and Pouce Coupé argued that there is the potential for competitive impacts with the use of a deferral. Pipelines that collect would be put at a competitive disadvantage to those that do not.

CAPLA submitted that the Board should not provide flexibility, such as a deferral, in the abandonment collection process, as landowners need to be protected. Immediate commencement of collection reduces risk for landowners because it spreads the burden of abandonment funding over the remaining economic life and allows companies to take greater advantage of compounding interest on the funds.

In addressing the risks of a deferral raised by other parties, Enbridge acknowledged that collection over a longer period could mitigate some of the risk of intergenerational inequities. However, it submitted that a longer collection period leads to other costs and risks. The first is increased risk of over-collection from early shippers as a result of estimates being less reliable at

that time. Second, a longer collection period can lead to a higher administrative burden with little or no corresponding benefit. Third, the benefits of compound interest from a longer collection period would need to be weighed against the opportunity cost to shippers of putting those funds to alternative uses.

In response to concerns that deferral could result in the under-collection of funds, Enbridge stated that while a deferral would shorten the time of collection, the real issue would be whether there would be a sufficient period remaining to collect the appropriate amount of abandonment funds. Enbridge envisioned a process to allow a company to apply for a deferral that would include adequate checks and balances under Board oversight so that it would not lead to greater risk of insufficient abandonment funds.

Enbridge argued that the concept of deferral should not be dismissed based on hypothetical situations. Instead, individual applications for deferral should be evaluated on a case-by-case basis.

Nominal Amount

TransCanada envisioned the need for an abandonment cost study to be completed after Stream 4, in order to estimate abandonment costs. In the meantime, TransCanada recommended beginning collection with a nominal amount in order to commence collection of abandonment funds before LMCI Stream 4 is complete. This nominal charge would not be based on any specific assumptions regarding the scope of pipeline abandonment and would be intended to get the process of collecting abandonment funds started in order to make a meaningful step towards addressing the issue of pipeline abandonment funding. The benefit of the nominal charge is that steps could be taken in parallel with Stream 4. However, TransCanada suggested that three issues would need to be resolved before any collection (including collection of a nominal amount) begins. These issues are: toll settlements in which shippers have agreed to a toll; the establishment of a mechanism to set aside funds; and tax efficiency of collections.

Enbridge submitted that it does not believe that a nominal collection is the appropriate starting point, as collection should be based on some reasonable understanding of the assumptions underpinning the collection amount. Westcoast submitted that any surcharge, whether nominal or not, would be premature.

KMC was also of the view that nominal collection was not appropriate because abandonment can be dealt with in a timely manner. It suggested that there was no need for the collection of a nominal amount as it was unaware of the imminent abandonment of any pipeline. Instead, collection should be established in an orderly fashion.

CAPP stated that there was no need to rush into a temporary collection scheme or collect some nominal amount of money on an interim basis. Moreover, to do so could undermine the goal of establishing a sound and economically efficient trust structure. CAPP expressed concern that if abandonment fund collection started before tax efficiency was achieved, it would be more difficult to achieve tax efficiency (discussed further in section 2.5). Enbridge, KMC, Pouce Coupé and the Alberta Department of Energy supported this position.

CAPLA did not support the collection of a nominal amount as this provides an opportunity for pipeline companies to delay the establishment of abandonment cost estimates by claiming that something is being done in the interim.

Group 1 vs. Group 2 Companies

KMC submitted that there are some issues generic to both Group 1 and Group 2 companies and others that are likely to be specific to Group 2 and that these should be examined separately. In its view, Group 2 companies should develop a recommended mechanism to deal with the specific issues, which could include opting into the Group 1 mechanism.

Pouce Coupé stated that the distinctions between Group 1 and Group 2 companies are not helpful in determining whether to set aside money for abandonment purposes. Pouce Coupé submitted that while it is not necessary to have a separate dialogue with all Group 2 companies, it would make sense that Group 2 companies not be subject to the same rigorous process that may be required of a Group 1 pipeline entity.

CAPP suggested that the Board should have a dialogue with each Group 2 company regarding any requirement for the funding of abandonment costs before imposing a funding mechanism on these pipelines. Group 2 companies should have the opportunity to propose alternatives to the generic model set out for Group 1 companies.

2.4 Method of Collection

All parties who filed evidence submitted that, should the Board decide that pipeline companies are required to set aside funds to cover future abandonment costs, those funds should be collected through tolls. The main reason given for this position was that customers who benefit from the service provided by the pipelines should also bear the costs associated with the service. It was the position of Enbridge, KMC and Pouce Coupé that any collection should be through a toll surcharge.

Enbridge, KMC, Pouce Coupé, Westcoast, TransCanada and CAPP stated that if funds are collected through tolls, they should be collected separately from depreciation expense in order to keep the funds identifiable and distinct.

2.5 Fund Governance

Several parties made submissions related to aspects of governance of funds set aside for future abandonment activities. Submissions of parties are grouped under the following topic headings:

- segregation of funds;
- pooling;
- management of funds;
- access to abandonment funds;
- reporting requirements;

- tax treatment of funds; and
- leaving federal jurisdiction.

Segregation of Funds

Most parties submitted that any abandonment funds collected should be set aside and maintained in segregated accounts. Parties recommended that there be a specific account or trust for each pipeline, which would segregate the funds from creditors and from non-regulated businesses. Most indicated that the provisions of the trust and its reporting will make this segregation automatic so that it does not need to be addressed specifically.

Enbridge, CAPLA, and TransCanada suggested that funds should be maintained in separate trust accounts for each pipeline and that trust accounts be administered and maintained by the pipeline company with third party oversight or audit. CAPP submitted that any collected funds should be maintained in a separate trust account for each pipeline, administered by a third party, to ensure that the funds would be available when abandonment costs are incurred. Westcoast was not opposed to the use of dedicated trust accounts administered by a third party.

KMC proposed that the Board ensure the funds are:

- held in trust and used only for abandonment purposes;
- in a trust that is prudently managed;
- invested in a reasonably prudent way and that speculative investments and direct investments in a pipeline's own assets are prohibited;
- in a trust that is audited annually to ensure proper collection and investment;
- reviewed and adjusted for accuracy every five years; and
- attached directly to the pipeline asset, such that they remain available regardless of the solvency or existence of the underlying pipeline company.

Enbridge proposed that the funds collected for future abandonment costs could be insulated from non-abandonment purposes through a combination of segregated accounts, compliance reporting and regulatory oversight.

CAPP suggested that funds in the regulated portion of a company could be "ring-fenced" in a manner that would preclude access from creditors of the non-regulated portions of the company as well as from creditors of the regulated entity. It further noted that a third party trustee, with appropriate legislated requirements for allowing withdrawals, would help to "creditor proof" the funds.

Pooling

Pooling of collected abandonment funds, or a portion thereof, was one potential mechanism of setting aside funds mentioned in the Board LMCI Stream 3 Discussion Paper. The Board also asked information requests on the merits of pooling to address the risk of there being insufficient funds to cover a company's abandonment costs, for example, from under-collection or from

under-performance of invested funds. Pooling could also address the risk of orphan pipelines, that is, pipelines where the responsible pipeline company has become insolvent and cannot cover the abandonment costs.

There was a consensus among the pipeline companies that there is only a small probability of insufficient funding for pipeline abandonment. TransCanada indicated that the risk is very small that abandonment would occur before sufficient funds are in place. Most pipelines and CAPP submitted that there should be no pooling or partial pooling of abandonment funds. Many parties raised a concern that pooling leads to cross-subsidization of companies that may have been less prudent in abandonment fund collection by those who have ensured they have sufficient funds. Consequently, in their view, pooling would be inconsistent with regulatory principles of cost causation.

Dr. Mansell, an expert witness for Enbridge, also opposed pooling. He acknowledged that a benefit of pooling could be the creation of economies of scale in administrative oversight, and even, potentially, some market power in investing the funds accumulated. However, he warned that there were significant reasons not to pool, such as concerns about creating a moral hazard,² asymmetric information³ and cross-subsidization.

Dr. Mansell acknowledged that there could be merit in pooling for some small component of the eventual costs, such as the residual risks⁴, but indicated that the merit of an orphan fund mechanism may depend on how an abandonment fund collection system works over time. If the risk of orphaned pipelines is greater at the time the system is reviewed than it is now, then that might be the time to look at an alternative mechanism as opposed to designing a system upfront with that risk as a given (which may result in a different system and different behaviour). Other parties (for example, Enbridge, Pouce Coupé) submitted that the residual risk of under-funding was not large enough to warrant the use of pooling for even a portion of the funds.

CAPLA supported the use of pooling as an additional safeguard but emphasized the need for sufficient collection to fund abandonment obligations on a pipeline-specific basis.

Management of Funds

According to TransCanada, governance of a trust involves establishing its management and a framework under which it is managed. The pipeline company would be responsible for developing and governing any trust fund established, while day-to-day management of the trust would be left to fund managers who would act according to governance documents and be subject to trust law. With respect to investment restrictions on funds accumulated, TransCanada

2 Dr. Mansell defined moral hazard in the pipeline abandonment context as 'the creation of an incentive for companies in designing their pipeline to ignore, or worry less about, the relatively higher abandonment costs of a particular option because they can fall back on a pooled fund to cover any additional costs.' More generally, moral hazard refers to the possibility that the behavior of an individual or company will change if they are protected from the consequences of their action.

3 Dr. Mansell defined asymmetric information as referring to the situation where the managers of an orphan fund do not have as good as information as the companies that actually operate them in order to properly assess risks and uncertainties associated with abandonment, so as to properly assess the cost, or charge, to each contributor to the fund.

4 Residual Risk -The possibility that abandonment funds remaining at the completion of the pipeline life are not sufficient to cover the entire cost of the abandonment activities.

suggested the appropriateness of various investment instruments should be determined on the following principles: minimizing the cost burden, through maximization of fund growth opportunities within acceptable risk tolerances; and optimal governance of funds.

Pouce Coupé recommended that investments of accumulated funds should be restricted to low risk vehicles, comparable to the restrictions on pension funds. CAPP recommended that investment restrictions should be similar to those applicable to pension funds, which are set out in the federal *Pension Benefits Standards Act, 1985*. KMC also noted the similarities to pension fund guidance, and further suggested a prohibition on direct investments in the pipeline owner's debt or equity.

Enbridge suggested two potential guidelines for investment policies. The first alternative would be a restriction to low risk vehicles from the outset (for example, Treasury-bills or short-term notes). The other alternative could allow for a more balanced portfolio at the outset, with a gradual shift to a portfolio more heavily weighted in low risk investments as abandonment approaches. Enbridge suggested a further generic procedure could serve as an appropriate means of establishing investment policy guidelines.

CAPLA stated that the Board ought to have an oversight committee that would oversee all pipeline collections and that landowners be represented on such a committee. One role of the committee would be to ensure funds are collected and invested properly.

Pouce Coupé recommended that arm's length professional fund managers should administer the fund. Selection from qualified service providers should be by competitive tender process. Landowner groups and shippers should not participate in overseeing the trust. Other industry parties also did not see a role for landowners with respect to the governance of any funds collected.

Access to Funds

Most parties submitted that the Board should control access to abandonment funds. CAPP, Enbridge, KMC and TransCanada suggested an application to the Board, such as a leave to abandon application, pursuant to paragraph 74(1)(d) of the NEB Act, should be required before funds are withdrawn. KMC proposed that access to abandonment funds would be subject to an application to the Board indicating:

- facilities to be abandoned;
- forecast cost of abandonment project;
- environmental issues to be addressed;
- consultation activities undertaken by the company;
- technical and engineering issues; and
- commercial issues.

CAPP agreed that the time to access funds would generally be at the end of a pipeline's life, however some abandonment activities may take place over time and access to the funds for these

would be appropriate. CAPP, Enbridge, Pouce Coupé and KMC recommended that access to the funds would be at the end of the pipeline's life. CAPP, Enbridge and Pouce Coupé also indicated that access to the abandonment funds should take place as abandonment occurs.

TransCanada submitted that abandonment would occur over time, and so funds may be required prior to actual physical abandonment, but access would be pursuant to a 'leave to abandon' order. It suggested that this would defer the question of whether interim retirements or only final abandonments could access the abandonment funds to consideration of individual paragraph 74(1)(d) applications.

Enbridge suggested access to funds would be through an order of the Board upon receipt of an application for abandonment. Access to funds would occur when the abandonment costs are incurred and this could be at one time or over a period of time. Enbridge agreed with TransCanada that large, complex pipeline abandonments would be a process over time, not one taking place at a point in time. Enbridge did not propose that pipelines have access to these funds for other purposes, such as for capital projects, operating and maintenance expenditures or during insolvency.

Pouce Coupé submitted that, at least for Group 2 companies, access to abandonment funds should be at the discretion of the pipeline company, and in accordance with the terms of the trust's constating documents and any regulatory requirements. It further recommended that companies should be required to report annually to the Board all such uses and be subject to the Board's audit process. Pouce Coupé described Board regulatory oversight as including: assessing the reasonableness of abandonment costs over time through periodic reviews; using existing regulatory approval processes; and being subject to a stakeholder complaints process.

Reporting Requirements

Some parties recommended that there be standard reporting requirements with respect to funds collected. Enbridge, KMC and Pouce Coupé each recommended requirements with basic information reporting, such as trust or account opening and closing balances; collections, income and other additions to the trust or account; and withdrawals or payments from the trust or account.

CAPP recommended standard basic reporting requirements and any additional reporting requirements agreed to between pipeline companies and stakeholders, for example:

- annual or semi-annual reports to the Board and to the stakeholders of the pipeline company;
- amount of funds collected over the reporting period;
- a report from the trustee including the cumulative amount in the trust, the earnings in the trust, the investments of the trust accounts (similar to what a pension manager would provide);
- gains or losses in the account;
- approximate percentage of amounts in trust or account relative to the most recent estimate of ultimate cost of abandonment; and

- amount of funds withdrawn or sought to be withdrawn together with NEB approval order or application number.

Tax Treatment of Funds

All industry parties noted that current tax laws do not allow a tax deduction for funds set aside in a reserve account for future abandonment costs. For full costs to be recovered from users of a pipeline system, a grossing up to a pre-tax basis for any dollar set aside for future abandonment costs would be required. For example, CAPP stated that, at a 33 per cent tax rate, tolls would need to collect \$1.49 for every dollar put into a trust or account unless the *Income Tax Act* is changed.

TransCanada suggested that the Board request the Department of Finance put in place an efficient tax treatment such that the funds collected to cover the cost of pipeline abandonment and contributed to a fund be allowed as a tax deduction in the year contributed. Money withdrawn from the fund would be included in taxable income, offset by tax deductions of abandonment costs incurred during the year.

CAPP recommended a model similar to Qualifying Environmental Trusts as defined in the *Income Tax Act* for mining and waste management companies required by their regulator to set aside funds for reclamation. CAPP further argued that the Board had a statutory obligation, under Part II of the NEB Act, to pursue changes to the *Income Tax Act* to increase the tax efficiency of collecting and setting aside funds for abandonment. CAPP argued that abandonment has a safety aspect to it. In its view, Part II of the NEB Act, paragraphs 26(1)(b) and 26(1.1)(b) imposes requirements on the Board to study, to keep under review the safety of pipelines, and to "report ...such measures within the jurisdiction of Parliament as it considers necessary or advisable in the public interest for...the safety of pipelines..."

Westcoast submitted that it supported the tax relief proposal by CEPA.⁵ According to Westcoast, under CEPA's proposal, withdrawals from the trust would be taxable at the time taken but would be offset by asset retirement expense. Income earned within the trust would be tax deferred until withdrawn from the trust.

KMC submitted that taxation issues could be addressed by seeking tax-exempt status for both the funds collected in a qualifying fund and earnings on the fund. While recognizing that tax issues are beyond the Board's jurisdiction, Pouce Coupé stated that the Board could play a role in facilitating legislative change.

Leaving Federal Jurisdiction

In the List of Issues, the Panel identified the issue of the handling of any funds collected to abandon a pipeline regulated by the NEB if the pipeline became subject to provincial jurisdiction, either after abandonment or through a transfer to a provincially regulated company.

⁵ Canadian Energy Pipeline Association submission dated August 14, 2007 to the House of Commons Standing Committee on Finance entitled "A Proposal to Grant Current Tax relief for Pipeline Abandonment Funding."

All parties who made submissions on this topic submitted the funds should follow the pipeline, and if a pipeline moves to provincial jurisdiction, a Provincial regulator should then have discretion over the funds.

Pouce Coupé noted that the NEB could handle abandonment decisions in such a way that it would not lose jurisdiction before abandonment funds are deployed, and that terms and conditions could be placed on a trust to ensure funds can only be used for specific purposes. Finally, it argued that the Board would not necessarily lose jurisdiction over a federal pipeline after an abandonment order is effective, and cited sections 49, 51.1 and 12 of the NEB Act as authority.

CAPLA submitted that MH-1-96⁶ and other cases decided by the Board are clear that the Board will no longer have jurisdiction after abandonment and cannot address post-abandonment impacts.

2.6 Risk and Uncertainty

The List of Issues set out a number of questions related to risk and how best to manage or mitigate the risks and uncertainties inherent in determining future abandonment costs and revenues. This topic included consideration of who should bear the risk and reward of trust account performance, and the risk and reward of under- or over-collection of funds.

CAPLA emphasized the need for “sufficient resources” to be available, stating that it is landowners who bear the risk of potential liability and costs resulting from under-collection unless other provision is made. CAPLA contended that the purpose of this proceeding is to ensure that the residual risk of a funding deficiency has been addressed, in order that landowners do not continue to bear this risk. CAPLA emphasized that steps must be taken to ensure that there is zero risk for landowners and that these steps must be taken to eliminate the risk to landowners irrespective of the cost and impact that taking those steps might have on pipelines and their shippers. It further noted that commencement of collection now rather than later reduces risk for landowners because it spreads the burden of funding over the remaining economic life and allows for the compounding of interest on the funds.

Most of the pipeline companies submitted that regular reviews of the estimates of the funds required for abandonment and the amount of funds collected would mitigate the risk of inaccurate estimates and insufficient funding. These parties testified that regular reviews were sufficient mitigation for the uncertainties related to funding future activities, as long as the pipeline is in operation. Residual risk was expected to be very minor.

CAPP submitted that addressing risks and uncertainties would be an ongoing process as the methods for physical abandonment are developed and refined, and technology is advanced. As a pipeline approaches the point of abandonment, the forecast of the cost to abandon the pipeline would become more accurate. The amount to be collected through the tolls to pay for the abandonment would be adjusted, pursuant to regular reviews. Therefore, the funds collected

6 National Energy Board, MH-1-96, Reasons for Decision, Manito Pipelines Ltd. (Facilities Abandonment), July 2006, page 21.

would approximate the forecast cost and the difference should not be significant. As a result, CAPP contended it was unnecessary to address this risk now.

Enbridge proposed that a suitable periodic assessment and adjustment process would mitigate risk of trust fund performance by re-evaluating underlying assumptions. Enbridge also submitted that it is not practical to eliminate risk 100 per cent. Enbridge contended that there is not sufficient cause for the Board to require pooling even of a portion of abandonment funds, to address the minute residual risk.

KMC recommended conducting reviews at least every five years for changes in abandonment technology, regulatory requirements, inflation, materials, labour and other cost-related factors. TransCanada submitted that periodic reviews to update expected terminal abandonment costs and abandonment timing and to take stock of the realized returns on fund investments would allow for adjustments to the funds collected. This would minimize any surpluses or deficits at the time of terminal abandonment.

Generally, parties submitted that there should be symmetry regarding the risk of under-collection and the reward of over-collection, that is, the party that is accountable for the risk of inadequate funding would also benefit from any over-funding.

Pouce Coupé proposed that the risk or reward associated with under- or over-collection of abandonment funds (that is, the short-term variations) should be to the account of the shippers. Further, over- or under-funding (that is, the long-term uncertainty) should be to the account of the pipeline company. Contending that abandonment costs are operating and not owning costs, TransCanada proposed that abandonment funds be managed in a manner similar to pension funding, where the normal practice is for shippers to bear the inter-year risk and reward (beyond the test year forecast risk) and pipeline companies to bear the intra-year risk and reward (within the test year forecast risk). Deviations from standard risk sharing would be permitted by the NEB, in a similar manner as deviations related to pension costs.

According to CAPP, if any trust accounts established for abandonment are required to have investment restrictions to minimize the downside risk, then any reward generated by the trust should remain in the trust and be part of the funds available to pay for pipeline abandonment.

In Enbridge's submission, the pipeline company should bear the risk and reward of trust account performance, as it is responsible for the abandonment liability and is well positioned to manage and mitigate the risk. The shippers on the pipeline should bear the risk and reward of under- or over-collection of funds.⁷

⁷ Enbridge defined under- or over-collection of funds as circumstances in which a pipeline company collects less or more on an annual basis than is required to be collected, as determined by the annual contributions to the abandonment fund that are necessary to fulfill the ultimate abandonment cost obligation.

2.7 Jurisdiction

Issue 7 of the List of Issues asked:

What is the Board's mandate under the current legislation to require the collection of abandonment costs as a component of a company's revenue requirement?

Many of the parties provided brief submissions on the jurisdiction issue. No party argued that the Board did not have authority to require the collection of abandonment costs as a component of a company's revenue requirement.

Citing subsection 48(2) of the NEB Act, KMC stated that the NEB has the mandate to require collection of abandonment costs as a component of a company's revenue requirement.

Pouce Coupé submitted that under Part IV of the NEB Act, including sections 59 and 62, the Board has broad discretion in the setting of tolls and tariffs for companies it regulates and that discretion is broad enough for the Board to require collection of abandonment costs by those companies. While stating that differing methods could be used for the determination of just and reasonable tolls, it submitted that the Board should adopt a single consistent method for any requirement to collect abandonment costs by those companies. Such an approach is least likely to impair the competitive position of any individual pipeline company relative to others.

Pouce Coupé further submitted that the Board has authority to direct that funds collected through tolls "be deposited into an abandonment trust fund or segregated account" and to set or require "any necessary terms of such trusts". However, in its view, the Board does not have jurisdiction to oversee pooled funds, including managing an orphan fund or directing surplus funds flow outside the scope of the Board's jurisdiction.

Westcoast submitted that the Board was mandated by its public interest obligation to balance conflicting interests and arrive at a judgment that is the best or most favourable for the overall public interest.

TransCanada stated that a fundamental premise of the Board's regulatory mandate is that all costs of service should be borne by those parties using the service, and the ultimate abandonment of facilities is part of that service. Further, TransCanada stated that based on the Board's clear jurisdiction over abandonment and the unrestricted definition of "tolls", it seems clear that the collection of abandonment costs is within the Board's jurisdiction and mandate. In addition, TransCanada adopted the submissions from Westcoast concerning the Board's public interest obligation.

CAPLA submitted that it was clear that the Board not only has jurisdiction over the abandonment of pipeline facilities but it also has the discretion to implement regulations that govern the abandonment of pipeline facilities for the protection of landowners from both safety and financial perspectives.

Chapter 3

Views of the Panel

3.1 Jurisdiction

During the RH-2-2008 proceeding, few parties addressed in detail the issue of the Board's jurisdiction to require collection of abandonment costs as a component of revenue requirement (thus making it possible for companies to apply to collect these costs from shippers through their tolls). As summarized in the previous chapter, many took no issue with the Board's jurisdiction to require collection of abandonment costs as a component of a company's revenue requirement. Several parties noted the Board's broad mandate set out in Part IV of the NEB Act, citing the following provisions in the NEB Act.

Section 59:

The Board may make orders with respect to all matters relating to traffic, tolls or tariffs.

Section 62:

All tolls shall be just and reasonable, and shall always, under substantially similar circumstances and conditions with respect to all traffic of the same description carried over the same route, be charged equally to all persons at the same rate.

The Panel notes that the Board's authority to determine just and reasonable tolls is not limited by any statutory directions. Courts have interpreted the provisions above to give the Board a very broad mandate to act on matters relating to traffic, tolls and tariffs.

Under it [Part IV of NEB Act], tolls are to be just and reasonable and may be charged only as specified in a tariff that has been filed with the Board and is in effect. The Board is given authority in the **broadest of terms to make orders** with respect to all matters relating to them [tolls]. Plainly, the Board has authority to make orders designed to ensure that the tolls to be charged by a pipeline company will be just and reasonable. But its power in that respect is not trammelled or fettered by statutory rules or directions as to how that function is to be carried out or how the purpose is to be achieved.⁸

In the Panel's view, the authority set out in Part IV of the NEB Act is sufficiently broad to allow the Board to embark on the inquiry, and issue a decision on whether the Board should require the collection of abandonment costs as a component of a company's revenue requirement. If the answer is in the affirmative, the Board would then be able to determine whether the collection of

⁸ *British Columbia Hydro & Power Authority v. Westcoast Transmission Co.*, [1981] F.C.J. No. 32, (FCA), at para 17, recently affirmed in *TransCanada Pipelines Ltd. v. Canada (National Energy Board)*, [2004] F.C.J. No. 654 (FCA) at para 30.

specific abandonment costs through tolls is a necessary component or requirement of just and reasonable tolls for a particular pipeline company.

Pouce Coupé also argued that the Board continues to have post-abandonment jurisdiction over pipelines. CAPLA argued that the Board does not have jurisdiction post-abandonment. The Panel notes that the Board is dealing with this issue in Stream 4 of the LMCI, and has released an advisory letter clarifying the Board's jurisdiction post-abandonment, dated 2 February 2009.

3.2 Key Principles and Considerations

Upon consideration of all the evidence in this proceeding, the Panel finds that it is an appropriate time for the Board to deal with abandonment funding in a principled manner. The sections that follow discuss key principles and considerations and a framework for moving forward.

In its 25 February 2008 letter regarding the LMCI Approach, the Board indicated that one of the potential outcomes of Stream 3 is that the Board would develop a set of principles that would guide it in its future decisions with respect to financial matters related to pipeline abandonment. The Panel reaffirmed this potential outcome in its first ruling on amendments to the List of Issues and Timetable of Events, dated 21 April 2008.

Also in its February 2008 letter, the Board set out two key goal-oriented principles as being fundamental to its future decisions with respect to financial matters related to pipeline abandonment. After careful consideration of the record in this proceeding, this Panel has reaffirmed these goal-oriented principles and has recommended additional key principles.

The Panel believes that the following principles and considerations will provide guidance to the Board in its future decisions in these matters. They are also intended to guide companies in addressing financial aspects of abandonment. Furthermore, all of these goal-oriented principles and considerations have been taken into account in the Panel's development of the Framework (described below) for setting aside of funds to cover the costs of abandonment and, as a result, the Framework strives to meet the goals set out in the principles.

The Panel is of the view that the implementation of the proposed Framework will be a significant step towards attaining these goals, in particular, through the regular review processes recommended therein.

The Panel recommends the following as key principles and considerations:

1. It is in the public interest that all pipelines regulated by the NEB be abandoned safely and effectively.
2. Pipeline companies are ultimately responsible for the full costs of constructing, operating and abandoning their pipelines, and the Board will hold the regulated company responsible for these costs.
3. The Board regulates using a goal-oriented, risk-based lifecycle approach; it does not subscribe to the concept of elimination of risk.

4. Landowners will not be liable for costs of pipeline abandonment.
5. At this time, the use of pooling as a general mechanism for setting aside funds to cover the costs of abandonment is not efficient from a regulatory or economic perspective.
6. Timing of abandonment of a pipeline for the purpose of estimating future abandonment costs should be the shorter of anticipated economic life or physical life.
7. The removal of all large-diameter abandoned pipe from agricultural land is not a prudent or effective approach for the purpose of establishing preliminary abandonment cost estimates.
8. Abandonment costs are a legitimate cost of providing service and are recoverable upon Board approval from users of the system.
9. Funds for abandonment costs should be collected and set aside in a transparent manner.
10. Funds for abandonment costs should not be collected as part of depreciation and should be a separate element of cost of service.
11. Any funds set aside for abandonment must be held in such a manner that they can only be used for the purposes of abandonment and abandonment planning.
12. The Board, as an independent and quasi-judicial tribunal, does not promote the development of tax policies or initiatives.

3.3 Discussion of Key Principles and Considerations

3.3.1 Principles relating to the Board's General Mandate

In order to have all pipelines regulated by the NEB abandoned safely and effectively, regardless of ownership of the facilities, there must be adequate funds set aside to cover all abandonment activities. In the Panel's view, pipeline companies are ultimately responsible for the full costs of constructing, operating and abandoning their pipelines. The Board will hold the regulated company responsible for these costs.

There are a number of methods by which the Board could hold a company responsible and seek to ensure that adequate funds are set aside for abandonment. For example, in addition to the Board's jurisdiction under Part IV of the NEB Act previously discussed, in the Panel's view, the Board also has a broader mandate within which it may consider funding of future abandonment costs. This consideration may fall within the Board's consideration of the present and future public convenience and necessity when a company seeks approval for a project under Part III of the NEB Act. It may also fall within the Board's authority with respect to providing for the protection of property and the environment. As a result, the Panel is of the view that the Board has regulatory authority to ascertain whether there are adequate funds set aside for the

abandonment of facilities it regulates, and to impose or enact additional regulatory requirements that endeavor to ensure such funding.

While these key principles apply to all companies regulated by the NEB, the details on how each company collects or sets aside funds for abandonment activities may differ. For example, Group 1 and Group 2 companies may have different methodologies for setting aside funds, and certain Group 2 companies may not collect funds from users if they do not have third-party shippers. Should a Group 2 company that does not charge tolls propose a methodology other than collecting future abandonment costs through tolls, the Panel recommends that the Board consider whether the alternative methodology ensures that adequate funds are set aside for abandonment costs and meets the goal of holding the pipeline company responsible for the full costs of abandoning its pipeline system.

The Panel notes Westcoast's submissions, which are summarized in Chapter 2, on excluding, at a minimum, Westcoast from any regulatory requirements to set aside abandonment funds for its gathering and processing facilities. There was no evidence presented at the hearing that persuaded the Panel that Westcoast, or any other company, would be unable to provide a preliminary estimate of abandonment costs. It is clear that the provision of preliminary estimates requires the use of a number of assumptions, some of which will be refined over time. This may result in adjustments to the estimates and, potentially, the collection methodology. However, the need to use assumptions rather than actual numbers is not sufficient rationale for not embarking on the exercise. In order to assist companies, the Panel recommends that companies use the Base Case assumptions set out in the Framework, discussed below, if companies are not able to determine reasonable pipeline-specific assumptions to calculate their own specific preliminary estimates.

The Panel notes that companies may have different proposals for collection or setting aside of funds. The Panel recommends that the Board remain open to companies submitting different proposals based on the facts of their particular facilities. It is also recommended that the Board exercise its discretion whether to approve or deny such proposals, including proposals regarding the timing of collection or setting aside of funds. The Panel recommends that the discretion be based on pipeline-specific information before the Board, including estimated costs to abandon those particular facilities, rather than estimates that rely extensively on the Base Case assumptions. This will provide the Board with the best information upon which it can make its determination.

3.3.2 Principles relating to Risk

The Board's regulatory oversight role applies to the entire lifecycle of a pipeline or facility. Using a goal-oriented approach to regulation, the Board defines desired outcomes, but allows companies to decide how best to achieve these outcomes throughout the lifecycle of the pipeline or facility. Companies are accountable for their own performance and are expected to identify and manage risk throughout a facility's lifecycle.⁹

⁹ This approach is more fully described in the Board's Annual Report 2008, available at <http://www.neb-one.gc.ca/clf-nsi/rpblctn/rprt/nlrprt/nlrprt-eng.html> at pages 5 and 6

The Panel does not believe that it is practicable for regulated companies to eliminate all risk no matter what the cost, as was submitted by CAPLA. At some point on the continuum of possible risks, a point of diminishing returns is reached, where the cost of trying to eliminate all risk is out of proportion to the incremental benefits that might result. However, the Panel reiterates that one of the goals reflected in the principles of the Framework is that landowners will not be liable for the costs of pipeline abandonment.

The Panel recognizes that currently there may be some risk of unfunded or underfunded abandonment. However, with respect to the risk of unfunded abandonment, no evidence was submitted during the proceeding that persuaded the Panel there were pipeline systems anticipated to be abandoned in the foreseeable future. As a result, it is not necessary for abandonment funds to be set aside immediately; there is time to establish a proper framework. Concerning the risk of underfunded abandonments, the Panel is of the view that over time these risks can largely be mitigated. As discussed in the Framework, there will be appropriate mechanisms in place to review abandonment cost estimates, and the accumulation of funds and growth of funds over time. These regular reviews will also mitigate the over-collection of funds from users, thereby ensuring a responsible approach to funding abandonment. The Panel also recommends that there be appropriate ongoing oversight by the Board of abandonment funding. In addition, the Panel notes that pipeline companies have an incentive to set aside and recover sufficient funds from their users so that they, and their shareholders, are not left with the responsibility for any shortfalls. All of these factors will help mitigate the risks of underfunded or unfunded abandonment.

The concept of pooling was raised during the hearing as a possible mechanism for setting aside abandonment funds or to address residual risk. After considering the views of parties, the Panel finds that the use of pooling, as a general method of setting aside the full costs of abandonment, would not be a prudent regulatory instrument at this time. In addition, using current resources to develop an appropriate pooling mechanism as a method of managing any small residual risks associated with unfunded or underfunded pipelines would not be efficient from a regulatory or economic perspective.

In the Panel's view, Board and company resources would be better directed to addressing other fundamental aspects, such as determining preliminary estimates and developing appropriate mechanisms to set aside adequate funds for abandonment. The Panel does not consider that there is currently a need to develop a stand-alone pooling mechanism to address either abandonment funding as a whole or residual risk. However, the Panel notes the Board's broad authority over abandonment funding and recommends that the Board not foreclose the possibility of implementing pooling mechanisms or contingency planning of some sort in the future.

3.3.3 Principles relating to Assumptions

One of the fundamental aspects to be determined by all companies is their preliminary estimates of the amount of funds needed to be set aside now, and on an ongoing basis, to cover the costs of abandonment. The assumed timing of abandonment of a pipeline is critical to this estimate. In the Panel's view, using a range of reasonable timeframes within which abandonment could occur may be a way to address uncertainties surrounding timing of abandonment, although there are likely other ways to deal with these uncertainties as well. Notwithstanding the various ways

abandonment timing could be dealt with, in the Panel's view, based on the evidence heard in the proceeding, economic life should generally be used to determine the timing (or ranges of timing) of abandonment rather than physical life. In the current market environment and given the ability of existing technology to extend physical life, it would be unlikely for physical life of a pipeline to be the determining timing factor. However, to accommodate those cases, the Panel recommends that timing for the purpose of calculating preliminary estimates on the amount of funds needed to be set aside should be based on the shorter of a pipeline's anticipated economic life or physical life.

Another key aspect critical to calculating preliminary estimates is the method of abandonment. As noted in the September 1985 Background Paper on Negative Salvage Value, there are three basic pipeline abandonment options available. These are removal, abandonment in place with continuing maintenance, and outright abandonment in place. In order to prepare their preliminary estimates of abandonment costs, many pipeline companies indicated that they needed guidance from the Board on the most appropriate abandonment standard to use. Several parties were of the view that it would not be possible to prepare their preliminary estimates until the LMCI Stream 4 process was completed, while CAPLA argued that its default technical assumption should be used for agricultural land.

The Panel recommends that the Board not wait until the Stream 4 process is completed before implementing the Framework discussed below. This Report sets out a number of high-level, goal-oriented principles related to certain technical assumptions to provide guidance to companies. In addition, the Framework is sufficiently robust to allow companies to begin work on their preliminary estimates, either by using the Base Case assumptions or their own pipeline-specific assumptions. The outcomes from LMCI Stream 4 may inform this process and feed into the ongoing processes for review over time, but it is not necessary to wait until the Stream 4 process is completed before any action is taken. The Panel is of the view that the preparation of preliminary estimates and the work planned for Stream 4 can proceed in parallel.

With respect to CAPLA's default technical assumption, the Panel was not persuaded on the evidence that removal of all large-diameter pipelines from all agricultural land is a necessary assumption. The Panel is of the view that in the absence of case-specific considerations, such as environmental, cost-related or risk-related considerations, mandated use of this assumption is not appropriate. Such a broad and general assumption would be neither prudent nor effective for establishing preliminary estimates of the costs of abandonment.

As a result, the Panel does not recommend use of this assumption as a Base Case assumption. However, it is within companies' discretion to use this assumption as they consider appropriate in preparing preliminary estimates of abandonment costs. Companies should use assumptions that make sense for the particular circumstances of their systems. The Panel recommends that pipeline companies be required to justify to the Board any assumptions used to calculate pipeline-specific preliminary estimates.

3.3.4 Principles relating to Collecting and Setting Aside Funds

With respect to a pipeline company's ability to collect funds to cover abandonment costs from its users, the Panel has stated in the key principles that abandonment costs are legitimate costs of

providing service and are recoverable upon Board approval from users of the system. In order to receive Board approval to collect future costs from users, pipeline companies are to come forward in a timely manner with a proposal for the collection of just and reasonable tolls, of which future abandonment costs will be a component. In each case, the Board will determine whether the funds sought to be collected are appropriately part of just and reasonable tolls for the regulated facility. For those Group 2 companies that do not charge tolls, alternative methods for setting aside abandonment funds must be developed and filed with the Board.

If companies do not submit proposals to collect these future costs from tollpayers or otherwise set aside abandonment funds in a timely manner, the Panel recommends that the Board identify other regulatory requirements that could ensure coverage of abandonment costs. Examples of other options may include the posting of bonds or letters of credit.

In order to meet the goal of ensuring that there are adequate funds to safely and effectively abandon pipelines, it is a fundamental principle that any funds set aside for abandonment must be held in such a manner that they will only be used for the purposes of abandonment and abandonment planning, and will not be available to third parties. To allow otherwise could increase the risk of underfunded or unfunded abandonments. Accordingly, the Panel recommends that all companies develop an appropriate mechanism to set aside funds to meet this principle. During the hearing, a number of possibilities were discussed, including a trust that provides restrictions in its constituting documents and setting up restricted access accounts. In their filings to the Board, as further discussed in the Framework, companies may propose any mechanism that, in their opinion, appropriately meets this goal, even if these mechanisms were not discussed during this proceeding.

The tax treatment of the funds collected and set aside for abandonment received considerable attention during the hearing. The Panel notes that parties raised no other proposals, other than changes to the *Income Tax Act*, that would result in a tax treatment satisfactory to industry parties for these funds. The Panel acknowledges that the tax treatment of abandonment funds will impact the amount of funding required to cover the costs of future abandonment activities.

Some parties suggested that the Board take a lead role in initiating changes to the *Income Tax Act*. CAPP went further and argued that the Board has a statutory obligation to increase the tax efficiency of collecting and setting aside funds for abandonment. It submitted that this statutory obligation stemmed from the Board's advisory functions with respect to safety of pipelines, pursuant to Part II of the NEB Act.

What was not clear from CAPP's argument was how the tax treatment of funds collected affects the *safety* of pipelines, particularly if the Board mandates collection of abandonment funds regardless of the tax treatment of such funds. Further, the Panel notes that no party, including CAPP, presented evidence that a safety impact is possible or might be realized in the absence of income tax changes. While the tax treatment may affect the willingness of the pipeline industry to collect funds or the amount that may be required to be set aside, based on the evidence presented to the Panel, there is no basis to make a finding that there is a connection between tax treatment of the funds and the safety of the pipelines themselves. Safety of pipelines is dependant upon physical aspects of the pipeline, and is overseen by the Board already through its regulation of the construction, operation, maintenance and abandonment of pipelines throughout

their life. Accordingly, the Panel was not persuaded that the Board is statutorily obligated to assist industry on this matter.

Furthermore, the Panel is of the view that the Board, as an independent and quasi-judicial tribunal, should not promote the development of tax policies or initiatives. Tax treatment of the abandonment funds that will be collected is an issue for the pipeline companies, working with others in industry, to pursue with the Department of Finance. As industry has submitted that changes in tax treatment are necessary, parties should endeavour to seek such change in a timely manner. However, as already noted, the funding of abandonment costs remains the responsibility of each pipeline company, regardless of tax implications. Tax efficiency is a goal of, not a deterrent to, the collection of funds for pipeline abandonment.

3.4 Framework

Given the above key principles and discussion, the Panel is of the view that it is now an opportune time to develop a framework to meet the goal of having adequate abandonment funds available for abandonment and abandonment planning when required. Setting aside of abandonment funds is required; however, it need not begin until some fundamental issues have been addressed and a framework has been implemented. This will allow accumulation of abandonment funds to proceed in an orderly fashion. The Panel is of the view that there is time to address certain outstanding issues and to implement a framework that will work for all pipeline companies regulated by the Board.

In reaching this conclusion, the Panel considered the following factors:

- No pipeline systems are anticipated to be abandoned in the foreseeable future.
- Applying the concept of risk management, as opposed to the concept of zero risk, parties did not present any evidence at the hearing that persuaded the Panel that time is of the essence in terms of the Board needing to require immediate collection or setting aside of funds.
- It would not be prudent from an economic efficiency perspective to implement a framework that results in the over-accumulation or under-accumulation of abandonment funds.
- In the Panel's view, the immediate collection or set aside of a nominal amount would divert resources away from tackling the fundamental aspects of abandonment funding.

Notwithstanding the recommendation to implement a framework applicable across the industry, pipeline companies are not precluded from filing an application with the Board to begin the collection or setting aside of funds for abandonment while the Framework is being implemented. If this should occur, the Panel recommends that the Board consider the application on its merits at that time.

In addition, the Panel notes that the Board is not precluded from considering the full costs of constructing, operating and abandoning a pipeline as part of its consideration of the present and future public convenience and necessity of a project when a company seeks approval under Part

III of the NEB Act, should the Board determine that doing so is appropriate based on the case before it.

Overview of Framework and Action Plan

It is essential that all regulated companies accept the responsibility for the full costs of their facilities, including abandonment costs. In the Panel's view, a fundamental element of accepting responsibility is the quantification, albeit approximate at this stage, of that responsibility.

Consequently, the Panel finds that pipeline companies are responsible for coming forward to the Board with estimates of funds needed for abandonment, justifying any assumptions used, and with proposals for the mechanisms and timing of the collection and setting aside of those funds. The ultimate goal is to have all companies begin to set aside funds to cover future abandonment costs no later than five years from the date of the decision of the Board. To achieve this goal, a number of steps must be completed within this five-year period, including the Board's assessment of filings. These steps are described below and summarized in Chapter 4, Action Plan and Base Case Assumptions.

The Panel recognizes that, should the Board adopt the proposed Framework and Action Plan, there will be increased regulatory interaction between stakeholders and the Board. This includes increased filings by companies within the next five years, resulting in increased assessments, and potentially hearings, by the Board over that same period with respect to those filings. Additional resources to hold and participate in at least one further technical conference will also be required. While these resources are not insignificant, the Panel is of the view that in order to progress on the issue of financial aspects of abandonment, an increased regulatory role, at least in the short to mid-term, is inevitable.

The Panel encourages all stakeholders to identify ways to increase efficiency, while respecting the key principles, the goals set out therein and ultimate goal of the Framework and Action Plan to ensure that funds are available when abandonment costs are incurred. Further, the Panel recommends that the Board also remain open to, and itself seek out, opportunities to increase regulatory efficiencies, even if acting on those opportunities results in refinements to the Framework and Action Plan.

Preliminary Estimates

As an essential first step, the Panel recommends that the Board direct each company under NEB jurisdiction (Group 1 and Group 2) to submit a preliminary estimate of its total future abandonment costs and the amount required to be set aside using basic assumptions regarding economic life and the method of abandonment.

To facilitate these submissions, the Panel has provided Base Case assumptions in this Report that companies may use to develop these preliminary estimates. A technical conference will be held to assess and discuss these assumptions. Following the discussion of these assumptions, and the issuance of a revised set of Base Case assumptions as necessary, each company will be expected to prepare and file an estimate of abandonment costs and the amount required to be set aside using the Base Case assumptions. Alternatively, should it not wish to rely on the Base Case assumptions, a company may file with the Board its pipeline-specific estimate of abandonment

costs for its pipeline system. The pipeline-specific estimate should be accompanied by discussion and supporting evidence for any assumptions the company is using that differ from the Base Case assumptions.

If a Group 1 company is using all of the Base Case assumptions, or if a Group 2 company is using either the Base Case or pipeline-specific assumptions, no approval is necessary for its preliminary estimates. If a Group 1 company is using any pipeline-specific assumptions, Board approval of the preliminary estimates is required.

The Panel recommends that Westcoast be required to calculate preliminary estimates for abandonment costs for its transmission (Zones 3 and 4) and its gathering and processing (Zones 1 and 2) facilities.

Collection of Funds

Group 1 companies would be required to file, for approval, a proposal for collecting the amount of funds required. Group 2 companies that charge tolls would file their proposals for collecting funds for abandonment. These proposals should contain discussion and justification of the time horizon and methodology for collecting future abandonment costs from users of the pipeline system.

Group 2 companies that do not charge tolls need not complete this step, but would be required to file with the Board their proposals for setting aside the amount of funds required (as discussed in the next step).

Concerning the method of collection, the Panel agrees with many of the parties who indicated that collecting abandonment funds should be transparent and this can be achieved for Group 1 or Group 2 companies that charge tolls through either tolls or a toll surcharge. However, there may be other transparent methods that companies wish to propose to the Board. The Panel is also of the view that abandonment funds should be separate from depreciation as an element of cost of service and that the funds should be segregated by pipeline.

Concerning negotiated toll settlements, the Panel's view is that within the timeframe established in the Action Plan, the majority of toll settlements will have expired. In the interim, in entering into new toll settlements, parties will be aware of this Framework and Action Plan. The Panel expects that parties will ensure that any new toll settlements address abandonment funding matters resulting from the Framework and Action Plan.

Setting Aside Funds

All Group 1 companies would be required to file, for approval, a proposed process and mechanism to set aside the funds. All Group 2 companies would file with the Board a proposed process and mechanism to set aside the funds.

The Panel recommends that any process and mechanism for setting aside the funds for abandonment have the following attributes:

- funds must be maintained in a segregated account and not be commingled with a company's general corporate funds;
- funds must be managed by an independent, third party;
- funds collected must be protected from creditors;
- funds must be protected from misuse or use for a purpose other than abandonment;
- regular reviews (at least every five years) of the amount of funds set aside and disbursed from the segregated account must be incorporated, and regular reporting to the Board and stakeholders must be built in;
- funds must be segregated by pipeline;
- funds must be subject to Board audit, as appropriate;
- companies must develop a sound investment policy for abandonment funds as ultimately, accountability for the collection and governance of the funds rests with each pipeline company; and
- the process for accessing the funds must be clearly set out in the mechanism.

Pipeline companies are expected to demonstrate to the Board how the mechanism they have chosen meets the goal of ensuring that adequate funds will be set aside to cover all pipeline abandonment activities. In the Panel's view, it is not necessary to use a one-size-fits-all approach. The market may play a role in determining the appropriate mechanism that a particular company may decide to adopt.

The Panel does not see a need to comment on the merits of the concept of deferral of collection or exemptions from collection or setting aside of funds. In the Panel's view, this is a level of detail beyond the scope of this proceeding, and is best addressed on a case-specific basis. As a result, this concept may form part of a company's proposal for collection and setting aside funds. However, as noted above in the Key Principles section, the Panel recommends that, as a prerequisite to considering any proposals to defer collection or set aside of funds, companies be required to submit information on a pipeline-specific basis, rather than using the Base Case assumptions. This will allow the Board to have before it the best information possible, upon which it may exercise its discretion to approve or deny such a proposal.

The Panel was not persuaded by CAPLA's submissions advocating the involvement of landowners in an oversight committee role to review abandonment funding. A role of such a committee requires a significant amount of time, resources and financial expertise. Further, given the key principles noted above, the ongoing Board oversight of this matter and that interested parties may participate in future NEB abandonment-related proceedings, the Panel does not recommend the establishment of an external oversight committee.

Access to Funds

As noted in Chapter 2, many parties in the hearing indicated that Board guidance on accessing the funds would be needed. In the Panel's view, funds should be accessible only for abandonment purposes. "Abandonment purposes" may include the development of an abandonment plan, as well as the undertaking of activities (for example, surveys and studies) to prepare an abandonment plan or to carry out an abandonment, and the continuation of post-physical abandonment activities (for example, monitoring or perpetual maintenance).

Pouce Coupé initially submitted that access to accumulated funds should also be permitted for decommissioning of facilities. Others argued that access should be restricted to covering abandonment, and abandonment process activities (such as pre-planning). The Panel notes that both deactivation and decommissioning contemplate continuation of system service. Provided service continues, revenue will be generated from the collection of tolls, from which funds should be available to cover these costs. Consequently, the Panel recommends that access to the funds should generally not be permitted for decommissioning or deactivation of facilities, unless the Board authorizes the access on the facts of a particular case before it.

Accordingly, in order to access the funds to cover costs of physically abandoning facilities and the costs for undertaking abandonment planning activities, companies will generally require a Board order, for example, pursuant to paragraph 74(1)(d) of the NEB Act.

As summarized in Chapter 2, Pouce Coupé argued that at least Group 2 companies should be able to access funds without a Board order. Instead, it submitted that Board oversight of the funds could be exercised through annual reporting of a company's access to the funds and audits by the Board of the funds. The Panel notes the expansive definition of "abandonment purposes" proposed herein, the requirement under the NEB Act to seek leave to abandon, and the recommendation that the Board exercise its discretion to authorize access in other circumstances as appropriate. Consequently, the Panel was not persuaded there is a need for a broad exception to the access procedure, such as the exception proposed by Pouce Coupé for Group 2 companies.

While the Board cannot mandate the process for accessing funds for abandonment of facilities that have fallen outside of the Board's jurisdiction, the Panel would recommend that companies consider, in the development of any mechanisms for setting aside the funds, the conditions for accessing funds should the related facilities fall within provincial or territorial jurisdiction at a later date. This may require sufficiently broad provisions or specifically-drafted provisions for access to encompass this potential situation. Exercising foresight on this issue now while developing appropriate mechanisms may save time and complications at a later date.

Chapter 4

Action Plan and Base Case Assumptions

4.1 Action Plan

Table 4-1 below summarizes the recommended steps going forward, along with the objectives, expected participants and timing of each step. The ultimate goal is to have all companies begin to set aside abandonment funds no later than five years from the date of the Board's decision. Companies that charge tolls would begin to collect funds for future abandonment costs no later than the first toll year following five years from the Board's decision. The deadlines proposed in the table are targets, and may be amended if the Board determines that circumstances require an adjustment.

Table 4-1
Action Plan

Action	Objective	Participants	Timing
1. RH-2-2008 Decision released	Discussion of principles, high level Framework, Action Plan, Preliminary Base Case	NEB	T (T equals release of NEB decision)
2. Board Technical Conference on Preliminary Base Case	Potential refinements to Preliminary Base Case	Group 1 and Group 2 companies that wish to attend, and any other interested person	T + 6 months
3. Release of Refined Base Case	Base Case issued for company use	NEB	T + 9 months
4. (a) Group 1 companies each prepare and file an estimate of abandonment costs and the amount required to be set aside using the Base Case assumptions OR (b) Group 1 companies each prepare and file, for approval , an estimate of abandonment	Filing of preliminary estimates using Base Case or pipeline-specific assumptions	Group 1 companies	No later than T + 24 months

costs and the amount required to be set aside using pipeline-specific assumptions or a combination of pipeline-specific and Base Case assumptions			
5. NEB consideration of Group 1 companies' preliminary estimates that use pipeline-specific assumptions or a combination of pipeline-specific and Base Case assumptions	NEB decisions on Group 1 companies' preliminary estimates	NEB	No later than T + 36 months
6. Group 1 companies each develop and file, for approval , a proposal for collection of funds and a proposed process and mechanism to set aside the funds [can be combined with step 4 and filed at T + 24 months]	Filing of proposed collection mechanisms and proposed set aside mechanisms	Group 1 companies	No later than T + 42 months
7. Group 2 companies each prepare and file an estimate of abandonment costs and the amount required to be set aside using either the Base Case or pipeline-specific assumptions	Filing of preliminary estimates using Base Case or pipeline-specific assumptions	Group 2 companies	No later than T + 30 months
8. Group 2 companies that charge tolls each develop and file a proposal for collection of funds [can be combined with step 7 and filed at T + 30 months]	Filing of proposed collection mechanisms	Group 2 companies that charge tolls	No later than T + 42 months
9. Group 2 companies each file with the Board a proposed process and mechanism to set aside funds [can be combined with steps 7 or 8, and filed at the earliest applicable date]	Filing of proposed set aside mechanisms	Group 2 companies	No later than T + 48 months
10. NEB consideration of Group 1 companies' proposals for collection and set aside mechanisms	NEB decisions on Group 1 companies' mechanisms for collection and set aside of funds	NEB	Within T + 5 years

4.2 Preliminary Base Case Assumptions

The Panel recommends that the Base Case assumptions in Table 4-2 form the basis for preparing preliminary cost estimates for each pipeline company. If pipeline companies choose to file their own pipeline-specific estimates of future abandonment costs, they should be prepared to justify any deviations from the Base Case assumptions that have been used in coming to these pipeline-specific estimates. These Base Case assumptions will be considered at a technical conference in approximately six months time, and all interested persons are invited to attend the conference. The Base Case assumptions will be refined shortly thereafter, if appropriate. The input of all parties will be considered in refining these Base Case assumptions.

Table 4-2
Base Case Assumptions

Method of Abandonment	See Table 4-3 below
Abandonment Cost Information	Use information in Oil and Gas Journal Survey filed by TransCanada ¹⁰ . Parties should explain how they used the data in this survey.
Economic Life	40 years (based on recommendations in the Canadian Institute of Chartered Accountants Handbook for estimating life of long-term capital assets)
Estimated Salvage Value	As no data was filed in this proceeding, and to be conservative, the Board has assumed zero
Inflation Rate	2 per cent (reflects Bank of Canada inflation target and approximates historical rolling averages)
Return on Funds Collected	4.5 per cent (based on Bank of Canada long-term bond yields, using those years between 2000-2009 when inflation averaged 2 per cent per year) ¹¹

Table 4-3
Method of Abandonment Assumptions

Land Use		Pipeline Diameter	
		Less than or equal to 203 mm (8")	Greater than 203 mm (8")
Agricultural	Crop	Assume 90% abandoned in place with no maintenance; 10% removed	Assume 80% abandoned in place with perpetual maintenance; 20% removed
	Pasture	Assume 90% abandoned in place with no maintenance; 10% removed	Assume 80% abandoned in place with perpetual maintenance; 20% removed
All Other		Assume 100% abandoned in place; 50% with perpetual maintenance, 50% with no maintenance	

10 Exhibit C-26-12, dated 29 January 2009, available at <https://www.nec-one.gc.ca/ll-eng/livellink.exe?func=ll&objId=546537&objAction=browse>

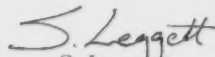
11 This 4.5 per cent per year is a nominal rate; combined with the 2 per cent inflation, it is 2.5 per cent per year in real dollars.

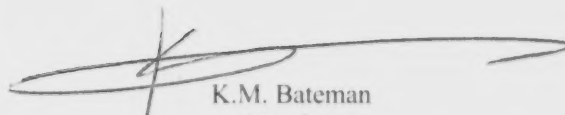
The above table is provided solely to start the discussion on these Base Case assumptions and the Panel expects that the numbers on this table will be debated in the forthcoming technical conference. While it recognizes that the number of categories for land use and pipeline diameter may be expanded and refined in the future and that every abandonment plan and pipeline-specific estimate will be case-specific, the Panel has recommended a simplified approach at this time due to the lack of information on the record of this proceeding. The split of agricultural land between crop and pasture recognizes that there will likely be different assumptions when those refinements are made.

Chapter 5

Recommendation

The section 15 Panel recommends that the Board accept the Panel's report, including the key principles, Framework and Action Plan.


S. Leggett
Presiding Member


K.M. Bateman
Member


L. Mercier
Member

Calgary, Alberta
April 2009

